

# One Minute Memo®



## FINRA Provides Guidance on Communications Regarding Unregistered Real Estate Investment Offerings

FINRA recently completed a review of communications relating to offerings of unregistered real estate investment trusts (“REITs”) and direct participation programs that invest in real estate (“DPPs” and together with REITs, “Real Estate Programs”). Noting a pattern of unfair, unbalanced and misleading communications in its members’ communications with the public regarding these Real Estate Programs, FINRA recently published Regulatory Notice 13-18 in May 2013 (the “Notice”) providing guidance on such communications. While, the Notice is targeted toward FINRA members such as investment banks and brokers who place securities of unlisted Real Estate Programs, the guidance provided is relevant and should be heeded by both public and private Real Estate Programs alike in connection with the preparation and distribution of offering documents.

The Notice references FINRA Rule 2210, which requires that a broker-dealer’s communications be fair, balanced and not misleading. The Notice provides the following examples of violations of Rule 2210 and remedial disclosure:

	Deficient Communication	Remedial/Compliant Disclosure
<b>General Disclosure</b>		
	Communications that imply investor is making a direct investment in real estate.	Clearly state that investment is in an entity that owns real estate assets or investments collateralized by real estate.
	Investment vehicle is a REIT, without qualification.	REIT status is pending and/or REIT status is subject to change.
	Risk disclosure in a footnote.	Risk disclosure in a clear and prominent manner commensurate with disclosure of benefits.
	Separately providing risk factors (even if communication is accompanied by a prospectus).	Include risk factors (or at least reference thereto) in all communications.
<b>Distributions</b>		
	Aggregating all types of distributions into a single amount or percentage.	Break out each type or component of distributions such as return of principal, proceeds from incurrence of indebtedness, equity offering proceeds or income from investments (and the time periods distributions have been constituted by each).  Explain that if distributions include a return of principal, the Real Estate Program will have less capital to invest.  Explain that if distributions are the proceeds of indebtedness, future distribution rates may not be sustainable and leverage adds additional risks.
	Describing the distribution rate as a yield similar to a fixed income instrument.	Explain that distributions are not guaranteed or fixed and are made at the discretion of the Real Estate Program.
	Inclusion of annualized distribution rate prior to two distributions that are equal to such rate for two consecutive full quarterly periods.	Disclose such rate only after it has been achieved for two consecutive full quarterly periods.

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<b>Stability/Volatility Claims</b>		
	Unfounded statements that the value of a Real Estate Program is stable or has limited volatility.	A sound basis for such claims must be provided (stability of the securities of the Real Estate Program is not an appropriate basis - as that does not indicate stability of the underlying assets).
<b>Redemption Features and Liquidity Events</b>		
	Unqualified discussion of redemption feature of the Real Estate Program.	Include explanation of any restrictions and limitations, such as the fact that the Real Estate Program may modify or terminate the ability to redeem.
	Unqualified discussion of liquidity event.	Include explanation that liquidity event is not guaranteed and/or may be altered at management's discretion.
<b>Prior Performance of Related Real Estate Programs</b>		
	"Cherry-picking" certain related Real Estate Programs.	Inclusion of results of all other affiliated Real Estate Programs.
<b>Use of Indices and Comparisons</b>		
	Citing performance of public REIT index to indicate performance of private REITs.	Only cite indices with underlying components that correspond to the Real Estate Program's portfolio.
	Unqualified use of an index.	Describe the components of the index and any relevant differences.
<b>Pictures of Specific Properties</b>		
	Use of pictures of properties owned by affiliates of Real Estate Program that are similar to the properties the Real Estate Program expects to purchase.	Include prominent text that such depicted property is owned by an affiliate and not the Real Estate Program.
	Use of pictures of properties which are collateral for investments of the Real Estate Program.	Disclosure that the property is collateral and not owned by the Real Estate Program.

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